85-872

No. .....

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1985

WILLIAM T. SCHOR and MORTGAGE SERVICES OF AMERICA,

Cross-Petitioners,

vs.

CONTICOMMODITY SERVICES, INC.

and

COMMODITY FUTURES TRADING COMMISSION,

Cross-Respondents.

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

(Cross-Petition to October Term, 1985 Nos. 85-621 and 85-642)

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November 18, 1985

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QUESTION PRESENTED

If the Commodity Futures Trading Commission has been constitutionally authorized to hear and decide a broker's state law counterclaim to a customer's Commodity Exchange Act claim, is the Commission also authorized to entertain the customer's state law claims in the nature of defenses, setoffs and counterclaims to the broker's counterclaim?

PARTIES TO THE PROCEEDING

The Commodity Futures Trading Commission adjudicated the claims of the parties in the administrative proceeding and was an appellee in the court of appeals. William T. Schor and Mortgage Services of America were complainants in the administrative proceeding and appellants in the court of appeals. ContiCommodity Services, Inc. was a counterclaiming respondent and an appellee in the court of appeals and Richard L. Sandor was a respondent in the administrative proceeding.

STATEMENT UNDER RULE 29.1

Cross-Petitioner, Mortgage Services of America, a New Jersey Corporation, is a wholly-owned subsidiary of The Howard Savings Bank, a New Jersey Stock Savings Bank Corporation. Affiliates of Mortgage Services of America are the other wholly-owned subsidiaries of The Howard Savings Bank which are: The Howard Federal Savings F.A., HOWCO Investment Group, The Howard Relocation Group, The Howard Insurance Group and HOWCO Residential Development, Inc.

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Cross-Respondents.

CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

William T. Schor ("Schor") and Mortgage Services of America ("MSA") respectfully cross-petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

This cross-petition is filed under Supreme Court Rule 19.5 and is a cross-petition to petitions for certiorari in:

ContiCommodity Services, Inc. ("Conti") vs. Schor and MSA, October Term, 1985, No. 642 filed on October 16, 1985 and received by counsel for cross-petitioners on October 17, 1985; and Commodity Futures Trading Commission ("CFTC") vs. Schor and MSA, October Term, 1985, No. 621, filed on October 11, 1985, and received by counsel for cross-petitioners on October 21, 1985.

OPINION BELOW

The first opinion of the court of appeals is reported at 740 F.2d 1262. It is reproduced in the Appendix to the Commodity Futures Trading Commission's Petition for Certiorari (October Term, 1985, NO. 621) to which this is a cross-petition at pages 8a through 49a (CFTC App., 8a-49a). The orders of the court of appeals denying the petitions for rehearing (CFTC App., 69a-70a) and the statement of two judges of the court of appeals dissenting from the denial of rehearing en banc (CFTC App., 71a-73a) are unofficially reported at 2 Comm. Fut. L. Rep. (CCH) ¶ 22,409. The decision of the Administrative Law Judge (CFTC App., 45a-55a) is unreported. The order of the Commission denying review of that decision (CFTC App., 50a-52a) is unofficially reported at [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,823.

The second opinion of the court of appeals on remand from this Court is reported at 770 F.2d 211. (CFTC App., 1a-7a).

JURISDICTION

The judgment of the court of appeals was reinstated on August 13, 1985 (CFTC App., 64a-66a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

This cross-petition is filed under Supreme Court Rule 19.5 and is a cross-petition to petitions for certiorari in: ContiCommodity Services, Inc. ("Conti") vs. Schor and MSA, October Term, 1985, No. 642 filed on October 16, 1985 and received by counsel for cross-petitioners on October 17, 1985; and Commodity Futures Trading Commission ("CFTC") vs. Schor and MSA, October Term, 1985, No. 621, filed on October 11, 1985 and received by counsel for cross-petitioners on October 21, 1985.

CONSTITUTION, STATUTORY PROVISIONS, AND REGULATIONS INVOLVED

Article III of the United States Constitution; Section 14 of the Commodity Exchange Act, 7 U.S.C. (& Supp. V 1981) § 18; the current version of Section 14, 7 U.S.C. § 18; Section 6(b) of the Act, 7 U.S.C. (1976 ed.) § 9; the current version of Section 6(b), 7 U.S.C. § 9; and 17 C.F.R. § 12.23 (b)(2) (1983), now codified at 17 C.F.R. § 12.19, are set forth at CFTC App., 74a-91a.

STATEMENT

This Statement amplifies, clarifies, augments and corrects the Statement in the Petitions for Certiorari to which

this is a Cross-Petition insofar as they bear on the question presented by this Cross-Petition.

First, it should be noted that the Congressional limitation of the jurisdiction of the CFTC in reparations claims to those based on violations of the Commodity Exchange Act, coupled with the CFTC regulation purporting to authorize state law counterclaims creates a possibility not present in cases brought in a court of general jurisdiction. That is the possibility of the original claimant having a claim against the respondent that could not be asserted initially but which would be either a defense, set-off or counterclaim to any state law counterclaim filed by the respondent. That possibility became a reality in this case.

Among the reparations claims made and defenses to Conti's counterclaims asserted by Schor and MSA were those based on the following facts. Schor's and MSA's trading accounts with Conti were under the required margin levels for at least six weeks prior to their being liquidated by Conti. This was so even though Schor and MSA met every margin call made by Conti throughout that period.

As a result of Conti's failure to liquidate the accounts when they first became undermargined, and Conti's failure to issue adequate margin calls sufficient to keep the accounts from being undermargined, Schor and MSA suffered serious losses part of which are represented by the trading account deficits for which Conti counterclaimed under Illinois law.

Before the CFTC and the court of appeals Schor and MSA argued these actions and omissions of Conti constituted breaches of Conti's duty to Schor and MSA under

state contract law. Therefore, they urged that, if Conti's state law counterclaims could be entertained by the CFTC, then the CFTC should decide the state law claims and defenses of Schor and MSA countering Conti's counterclaims.

The CFTC refused to consider these claims of Schor and MSA on the grounds that it had no jurisdiction over claims not based on violations of the Commodity Exchange Act or of CFTC regulations and these claims were not violations of the Act. The CFTC did entertain Conti's state law counterclaims. It did not even consider whether Conti's failures to require adequate margin and to liquidate the trading accounts when they became undermargined constituted a defense or setoff against Conti's counterclaims.

Atlhough the evidence was undisputed that Schor and MSA were undermargined for the six week period and that they met all Conti's margin calls during that period and Conti even agreed on the record that this was so, the CFTC Administrative Law Judge made no finding of fact or conclusion of law one way or the other regarding these facts.

The CFTC itself denied review of the ALJ's decision while stating that it "has neither adopted the Presiding Officer's order as its own nor affirmatively passed upon any of the issues decided therein." (CFTC App., 50a). The CFTC, in a footnote to its Order indicated that the procedure of having counsel for one of the parties prepare the ALJ's initial decision "be used, if at all, only in exceptional cases." (CFTC App., 50a).

The Court of Appeals did not reach the question presented in this Cross-Petition because it directed dismissal of Conti's counterclaims after finding that the Commodity Exchange Act, by its terms, does not authorize the CFTC to entertain state law counterclaims. The Court did note that the CFTC, despite advocating its authority to hear state law counterclaims, remains ambivalent on whether state law claims may be asserted against state law counterclaims. 740 F.2d at 1279, fn. 29.

Both Conti and the CFTC have now petitioned this Court for a writ of certiorari seeking a ruling that the CFTC was authorized by Section 14 of the Commodity Exchange Act, as it existed prior to being amended in 1983, to entertain state law counterclaims.

This Cross-Petition merely asks, that if the Court considers that question, that it also consider whether the CFTC should entertain state law claims asserted as defenses, setoffs and counterclaims to state law counterclaims.

———o———

REASONS FOR GRANTING THE WRIT

Should this Court grant certiorari on the Petitions of Conti and CFTC it should grant this Cross-Petition in order to have the full statutory construction and constitutional questions raised by Conti and the CFTC before it.

Simply put, if the Court decides that Congress intended the CFTC to entertain state law counterclaims, it must then decide the Article III constitutional question regarding the state law counterclaims which the Court of

Appeals did not reach. In deciding both of those questions the Court should also rule whether the CFTC may or must entertain state law claims by the original claimants asserted as defenses, setoffs and counterclaims to state law counterclaims against them.

All of the reasons Petitioners advance in support of their petitions apply equally to the question raised in this Cross-Petition.

Thus, Conti and the CFTC allege in their petitions that, if brokers cannot file state law counterclaims against customers, those customers will be deterred from using the CFTC reparations procedure. Of course, any such deterrent would be magnified manyfold if customers could only claim for Commodity Exchange Act violations, while their adversaries could counterclaim under state law knowing that the customer could neither defend, setoff nor counterclaim under state law. In fact, this is exactly what happened in this case prior to the decision of the court of appeals.

If the Court reaches the Article III question, it will have to resolve the main issue raised in the Conti and CFTC petitions; the issue of whether filing a CFTC reparation claim operates as an effective implied consent to the trial of state law counterclaims against the claimant by a non-Article III tribunal. That issue would even more strongly arise here, i.e., whether the filing of a state law counterclaim effectively implies consent to adjudication of state law defenses and counterclaims against the first counterclaim.

Petitioner's arguments based on the legislative history of the 1983 amendments to the Act (passed after this

case was decided by the CFTC) also apply here including the passage quoted in footnote 13 of the CFTC Petition to the effect that "the reparations program seeks to pass upon the whole controversy surrounding each claim". Clearly, the defenses to counterclaims and counterclaims to counterclaims form part of the "whole controversy."

Finally, petitioners have argued that this case comes within the "public rights" exception to the general Article III requirement that federal judicial power be exercised only by forums with the tenure and salary protections contained in Article III. Of course, if a state law counterclaim by a broker against a customer is within that exception, then state law defenses and claims asserted against the counterclaimant are also within the "public rights" exception.

For the Court's information, the defenses and counterclaims raised by Schor and MSA to Conti's counterclaims were based on a breach of contract by Conti and supported by two landmark cases dealing with the obligations and rights of commodity futures brokers and their customers.

In the first of these cases, *First Mid America, Inc. v. Palmer,* 197 Neb. 224, 248 N.W.2d 30 (1976), the customer, whose account had been liquidated for being under required margin was sued for the resulting deficit balance by his broker. The customer defended on the basis that the broker did not liquidate his account within a reasonable time after it became undermargined and this violated exchange rules which the broker had contracted to observe. The Court held that one cannot recover for losses caused by his own breach of contract and affirmed a judgment for the defendant customer.

The Customer Agreement here contains a provision virtually identical to the provision relied on in the *First Mid America* case. That case also involved regulations of the Chicago Board of Trade which was the exchange involved here.

The other case, *Iowa Grain v. Farmers Grain and Feed Co., Inc.*, — Iowa —, 293 N.W.2d (1980), held that a broker who did not liquidate a customer's account for being undermargined within twenty-four hours was liable for a breach of its contract to follow the same Chicago Board of Trade rule requiring margin.

Of course, here the delay in liquidating was at least six weeks and the delay was compounded by the inadequate margin calls made by Conti throughout that period which Schor and MSA met. The loss they suffered was the decline in value of their trading positions plus the margin calls they met during that period.

This case illustrates vividly the unfair position in which a customer-claimant in CFTC reparations is now placed. If the broker counterclaims under state law, the CFTC will hear that counterclaim but will not hear state law defenses and claims of the customer. That unfairness would be confirmed if this Court considers only the issue of state law broker counterclaims and does not at the same time consider customers' state law defenses and counterclaims.

The Administrative Law Judge indicated from the bench at the hearing that since these were not violations of the Commodity Exchange Act they could not be the subject of an award. However, in its brief before the court

of appeals Conti countered Schor's and MSA's breach of contract arguments by arguing that Conti had not breached the agreement.

Finally, this Court has previously denied a Cross-Petition for Certiorari filed by these Cross-Petitioners which was identical to the current Cross-Petition. *Schor v. ContiCommodity Services Inc.*, — U.S. —, 105 S.Ct. 3480 (1985). Such a prior denial of certiorari does not require the Court to treat the earlier disposition as final. *Washington v. Fishing Vessel Assn.*, 443 U.S. 658 at 672, fn. 19 (1979). See also *Brown v. Allen*, 344 U.S. 443 (1953), where the majority (per Frankfurter, J.) held that denial of a writ of certiorari should be disregarded in passing on a subsequent application for relief where, as here, no reason was given for the denial.

CONCLUSION

If this Court grants the petitions of the CFTC and Conti for Certiorari, it should grant this cross-petition so that all issues involving adjudication of state law matters by the CFTC will be decided and so that any decision it renders will be fair to both brokers and their customers.

Respectfully submitted,

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OCTOBER TERM, 1985

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v.

CONTICOMMODITY SERVICES, INC., ET AL.

ON CROSS-PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

MEMORANDUM FOR THE COMMODITY FUTURES TRADING COMMISSION IN OPPOSITION

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MEMORANDUM FOR THE COMMODITY FUTURES TRADING COMMISSION IN OPPOSITION

The Commodity Futures Trading Commission, in its administrative reparations forum, adjudicated both the cross-petitioners' claim against cross-respondent Conti-Commodity Services, Inc., under the Commodity Exchange Act (CEA), 7 U.S.C. 1 *et seq.*, and Conti's state law counterclaim against cross-petitioners.[1] Cross-petitioners now contend that the Commission should also have adjudicated their state law claim of breach of contract against Conti, the very claim that this Court declined to review last Term. *Schor* v. *ContiCommodity Services, Inc.*, cert. denied,

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[1]Cross-petitioners are respondents in both No. 85-621, *CFTC* v. *Schor*, and No. 85-642, *ContiCommodity Services, Inc.* v. *Schor*. The Court granted these petitions and consolidated the cases on December 9, 1985.

No. 84-1673 (June 17, 1985).[2] Cross-petitioners' contention does not merit review because they did not properly raise their state law claim in the administrative proceeding.

1. a. The background and facts of this case are stated in detail at pages 2-9 of the petition in No. 85-621. When cross-petitioners filed their reparations complaint with the Commission, alleging that Conti had violated the CEA and Commission regulations, Conti responded and filed its counterclaim. Cross-petitioners responded to Conti's counterclaim by filing a reply as permitted by Commission Rule 12.24, 17 C.F.R. 12.24 (1983).[3] But in that reply, cross-petitioners did not allege a breach of contract or any state law defense, setoff, or counterclaim. Rather, cross-petitioners simply renewed their claim that Conti had violated the CEA and the Commission's regulations. See C.A. App. 495-503.

The case was then assigned to an Administrative Law Judge. The parties filed motions, conducted discovery, and filed pretrial briefs. A three-day hearing was held before the

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[2]Following the denial of cross-petitioners' previous petition, the Court granted petitions filed by the CFTC and Conti, vacated the court of appeals' judgment, and remanded the case for further consideration in light of *Thomas* v. *Union Carbide Agricultural Products Co.*, No. 84-497 (July 1, 1985). *ContiCommodity Services, Inc.* v. *Schor*, No. 84-1500 (July 2, 1985); *CFTC* v. *Schor*, No. 84-1519 (July 2, 1985). On remand, the court of appeals reinstated its prior judgment. See No. 85-621 Pet. 8-9.

[3]Commission Rule 12.24, 17 C.F.R. 12.24 (1983), provides:

> If the answer asserts a counterclaim, the complainant shall file a reply to the counterclaim with the Commission within thirty * * * days after service of the answer. The reply shall be strictly confined to the matters alleged in the counterclaim, and shall in all respects conform to the requirements set forth in § 12.23(b) with respect to the form and content and other requirements concerning an answer. A complainant may satisfy a counterclaim, as if it were a complaint, in the manner set forth in § 12.23(a).

ALJ at which several witnesses testified. After the hearing, cross-petitioners filed their post-trial brief and proposed findings of fact and conclusions of law, and Conti filed its post-trial brief. Throughout this time, cross-petitioners never raised a state law breach of contract claim. See C.A. App. 558-559, 619-689.

In their reply brief to Conti's proposed findings of fact and conclusions of law, cross-petitioners, for the first time, asserted that Conti's counterclaim "must be dismissed" because Conti had breached its contract with cross-petitioners by allegedly failing to abide by exchange margin rules. C.A. App. 806. The ALJ then announced his decision, which rejected cross-petitioners' claim under the CEA but upheld Conti's counterclaim and directed Conti to draft a proposed order. Cross-petitioners filed extensive objections to Conti's proposed order but did not mention their state law breach of contract claim. See C.A. App. 858-868. Since cross-petitioners had raised the breach of contract claim only in this half-hearted and untimely fashion, and since that claim, as a result, had not been a subject of the evidentiary proceedings, the ALJ, unsurprisingly, did not address it.

b. Cross-petitioners applied to the Commission for review of the ALJ's decision. One of the grounds they urged was that the ALJ had not ruled on their breach of contract claim. C.A. App. 900-903. Conti, in its response, objected that cross-petitioners had not raised that claim before the ALJ. *Id.* at 928-930. The Commission denied review. 85-621 Pet. App. 50a-52a.

c. Cross-petitioners then petitioned for review of the Commission's decision by the court of appeals. In their brief in the court of appeals, cross-petitioners asserted that the Commission had acted "unfair[ly]" in refusing to entertain

their breach of contract claim. Cross-Pet. C.A. Br. 28-29. The Commission, in its court of appeals brief, responded that this issue had not been properly raised in the administrative forum and thus was not appropriate for consideration by the court of appeals. CFTC C.A. Br. 22-25. The Commission explained to the court of appeals that its regulations would permit a reparations claimant to raise a state law defense to a broker's counterclaim but that, under Commission procedures, cross-petitioners' failure properly to raise the claim in the reparations forum constituted a waiver. *Id.* at 24 n.28, 25; see 17 C.F.R. 12.24 (1983). The Commission further explained that the question whether a reparations claimant could file a state law counterclaim to a broker's state law counterclaim had never been ruled on by the Commission because it was not properly raised by cross-petitioners and, in fact, had never arisen in the entire history of the reparations program. CFTC C.A. Supp. Br. 18 n.14.[4] The court of appeals did not address cross-petitioners' contention that the Commission erred by not considering their breach of contract claim.

2. Cross-petitioners now contend that this Court should decide whether the Commission is "authorized to entertain the customer's state law claims in the nature of defenses, setoffs and counterclaims to the broker's counterclaim." 85-872 Pet. i. As cross-petitioners admit, "this Court has previously denied a Cross-Petition for Certiorari filed by these Cross-Petitioners which was identical to the current Cross-Petition." *Id.* at 10; see page 1, *supra*. Cross-petitioners offer no new reason for review.[5]

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[4]The court of appeals incorrectly suggested that the Commission is "ambivalent" on this question. 85-621 Pet. App. 44a. In fact, the question simply has never arisen, and the Commission accordingly has not had occasion to take a position on it.

[5]Neither of the cases on which cross-petitioners rely (Pet. 10) suggests that a party routinely may reapply for a writ of certiorari following the denial of a petition raising the same claim in procedurally identical

As we have demonstrated, cross-petitioners did not properly raise their state law breach of contract claim in the administrative forum. Review by this Court is therefore inappropriate. See, *e.g.*, *United States* v. *L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 37 (1952). Moreover, because of cross-petitioners' failure properly to raise their breach of contract claim, neither that claim nor cross-petitioners' contention concerning the Commission's authority was ever addressed by the ALJ, the Commission, or the court of appeals. That is an additional reason for this Court to deny review.

Indeed, cross-petitioners and the Commission may not even be in disagreement on the question presented in the cross-petition. That question refers to "defenses, setoffs and counterclaims," and cross-petitioners have never explained into which category their state law breach of contract claim falls.[6] But as the Commission explicitly stated in the court of appeals, the Commission agrees with cross-petitioners that it has the authority to consider state law defenses to brokers' state law counterclaims. There may, accordingly, simply be no dispute for the Court to resolve on this issue. As the Commission also explained in the court of appeals, and as we noted above, the Commission has never had occasion—in this case or in any other case in the ten-year history of the reparations program—to decide whether to

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circumstances. See *Washington* v. *Fishing Vessel Ass'n*, 443 U.S. 658, 672 n.19 (1979) (declining to treat as a final adjudication a prior denial of certiorari that "came at an interlocutory stage in the proceedings"); *Brown* v. *Allen*, 344 U.S. 443, 489-497 (1953) (opinion of Frankfurter, J., in substance expressing the views of the Court) (denial of certiorari on direct review in state criminal case should not be accorded legal significance by district court in subsequent habeas proceeding).

[6]That lack of clarity is directly attributable to cross-petitioners' failure to plead their breach of contract claim in response to Conti's counterclaim.

assert the authority to adjudicate reparations complainants' state law counterclaims to brokers' counterclaims.[7] The Commission had no reason to consider its authority to entertain cross-petitioners' state law claim because that claim was not properly raised. Plainly this Court should not decide the scope of the Commission's authority in this area when neither the Commission itself nor any court has taken a position on that issue.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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Deputy General Counsel

ANNE H. WRIGHT
Attorney
Commodity Futures Trading Commission

DECEMBER 1985

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[7]The Commission also has arrived at no view concerning setoffs in general, although some of what are called "setoffs" are in fact properly treated as affirmative defenses.